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# All of one kind? Labour market reforms under austerity in Italy and Spain

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## Abstract

Most scholars have highlighted the commonalities of labour market reforms under austerity in Europe, mostly in terms of liberalization. We argue that a more differentiated analysis is in order, as empirical developments point to distinct reform trajectories. We analyse in detail the two South-European cases where pressure for austerity was intense but governments maintained a degree of discretion as they were not subjected to direct bailout conditions: Italy and Spain. We examine the period since 2010, which includes a major labour market reform in each of the two states in 2012. Using a theoretical framework that allows distinguishing forms of liberalization, we find that reforms in the two states indeed differed markedly. In Spain flexibilisation and declining coverage of protection prevailed whereas in Italy flexibilisation was combined with improved protection of workers at the margin of the labour market. The differing influence of the centre-left helps to explain this divergence.

**Keywords:** labor market institutions, industrial relations, Europe, liberalization, crisis

**JEL classification:** **J08** (Labor economics policies); **J58** (Labor–Management Relations, Trade Unions, and Collective Bargaining: Public Policy), **J88** (Labor Standards: Public Policy)

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## 1. Introduction

The global economic and financial crisis that erupted in 2008 had not only massive repercussions on employment and unemployment but also on labour market policies and institutions. While initially the protection of workers was expanded in many countries, since 2010 the character of government interventions in the labour market changed. In Europe labour market reforms were seen as a key to regain competitiveness and to reduce government spending. The main research question in this article is whether there are any alternatives in the direction of labour market reforms that governments in Europe can pursue under austerity pressures. Most research has emphasized the commonalities of these reforms in terms of liberalizing labour market institutions. Drawing on Thelen's (2014) 'varieties of liberalization', we argue that this view must be differentiated. Italy and Spain both adopted significant reforms of labour market policy in 2012, at the height of the so-called sovereign debt crisis. As we will show below, the thrust of both reforms is markedly different. Spain is a clear example of deregulatory liberalization, while Italy combined flexibilisation with an increase in coverage of some protective institutions, especially unemployment benefits.

Given the structural and institutional similarities between Italy and Spain the differences we find between their labour market reforms in this phase are surprising. From the comparative analysis, we identify some preliminary evidence regarding what factors can explain the differences between the two reform paths. The similarities between both cases exclude many rival explanations and lead us to assert that the partisan composition of governments was instrumental. However, given the space constraints we cannot fully develop the causal argument in this article.

The next section situates this study in the context of the literature on labour market policy reforms during the Great Recession. We then discuss the theoretical framework, which we adapt from Thelen (2014), taking into account the specificities of Southern European countries and their welfare regimes. Subsequently, we explain the research design and provide an overview of pre-crisis labour market policy in Italy and Spain as well as their employment performance in the crisis. The following section contains the main comparative analysis and discussion of the labour market reforms adopted since 2010, while the final section concludes.

## 2. Labour market reforms under austerity – liberalization only?

In the first years of the global financial and economic crisis economic stimulus measures,

widened schemes of unemployment protection, and, especially, the financial bailing out of private banks increased the financial commitments of governments (Blyth, 2013). For many governments in the European Economic and Monetary Union (EMU) this led to market concerns about the viability of their sovereign debt as they lacked a lender of last resort to back up the debt (De Grauwe, 2011). Fiscal consolidation took centre stage in many European countries, especially Southern European ones, leading to the onset of the so-called ‘age of austerity’ (Armingeon and Baccaro, 2012). In line with its implicit use in most of the literature, we define ‘austerity’ broadly as a policy context of political pressures not only for fiscal consolidation but also for so-called ‘structural reforms’, i.e. recasting institutions to improve international economic competitiveness (Petmesidou and Guillen, 2014).

Most literature on labour market reforms under austerity tends to treat these as homogenous and characterizes them as instances of liberalization. The notion of liberalization as the characterizing feature of political-economic change in recent decades was famously advanced by Streeck (2008; 2011) and defined as a gradual expansion of market relations in areas previously reserved for democratic and collective decision-making. In the field of labour market policy, liberalization is often understood as a general weakening of the position of labour and an expansion of employer discretion through the decentralization of industrial relations, the shrinking of the collective organisational capacity of class actors and the dismantling of employment protection legislation (EPL) and of other protective institutions such as unemployment benefits (Baccaro and Howell, 2011). This has been identified as the defining characteristic of labour market reforms under austerity, as the search for new bases of capital accumulation in response to flailing economic growth and growing public deficits results in reforms designed to undermine the position of labour (Becker and Jäger, 2012; Heyes et al., 2012). Indeed, in the reform discourse it is often taken for granted that a decrease in EPL will bring about an increase in employment and competitiveness. Yet, such a relationship is far from solid as empirical research has shown (Amable et al., 2011; Avdagic and Salardi, 2013).

Moreover, labour market deregulation in Southern European countries is explained as a consequence of EMU drastically limiting the adjustment strategies available to national governments (Armingeon and Baccaro, 2012). As monetary policy is set by the European Central Bank (ECB) and fiscal policy is constrained by the Stability and Growth Pact, labour market flexibilization and wage moderation become the main adjustment mechanism available to domestic governments to improve competitiveness through ‘internal devaluation’. The economic governance tools introduced in the EU since the beginning of the crisis to regulate public debt and deficit— such as the European Semester, the ‘Six-Pack’, and the Euro Plus Pact — reinforce

this constraint. This is accompanied by a reform agenda focused on market-driven structural adjustment through wage squeezes, erosion of labour rights and weakening of public services (Bieling, 2012). Also for our two cases in particular, Italy and Spain, this type of liberalizing reform has been identified as the main reform trajectory after 2010 (Meardi, 2012; Petmesidou and Guillen, 2014; Koukiadaki et al., 2014; Pavolini et al, 2015; Hopkin, 2015).

Prior to the crisis, labour markets in much of Southern, Continental, and Central Europe have often been deregulated at the margins, facilitating non-standard employment, while leaving the protection of full-time permanent employment largely intact. As we set out below, Italy and Spain are indeed characterized by entrenched segmentation in their labour market and social protection, which for simplicity is often called ‘dualism’. The described comprehensive liberalization of labour market institutions, insofar as it affects also labour market ‘insiders’, can be seen as a break with the previous policy path. This view, however, is contested by some scholars (Bentolila et al, 2012; Dubin, 2012) who emphasize instead how, even in the presence of exogenous pressures for structural reforms, attempts to introduce greater labour market flexibility in dualized countries such as Italy and Spain still follow a trajectory of dualization, thus focusing structural adjustment primarily on the ‘outsider’ component of the workforce (i.e. non-standard workers and the unemployed), leaving protections of insiders more or less untouched. In these accounts, it has been argued that left parties and trade unions have managed to mobilise their power resources to defend the interest of insiders as their core constituency, acting as veto players and shifting the costs of structural labour market reforms primarily on outsiders (Rueda, 2012).

Analysing the fate of Southern European welfare states in the context of the post-crisis response, Petmesidou and Guillen (2014) ask whether the exogenous shock of the crisis has opened a ‘window of opportunity’ for Southern European countries to welfare state recalibration aimed at addressing long-standing structural imbalances of their welfare and labour market models (cf. Ferrera and Hemerijck, 2003). Whilst their own answer to this question is largely negative, Clasen and colleagues (2012) did identify this type of crisis response in countries with entrenched labour market dualism, such as in Southern Europe. Similarly, Leschke (2012) raised the expectation that the negative performance of Mediterranean welfare states in the crisis in terms of employment and poverty could have acted as triggers of institutional change, by putting the issue of labour market segmentation on domestic policy agendas. Therefore, while the major part of the literature has found labour market reforms under austerity to consist of liberalization, there are two minority views: one sees these reforms as continuing dualization, the other sees a window of opportunity for welfare state recalibration. Either way, most contributions to this

literature argue for one trend across countries.<sup>1</sup>

### **3. Varieties of liberalization in labour market reform**

The accounts referred to above use one of three concepts that are widely established in the Comparative Political Economy literature: liberalization, dualization, or recalibration. These concepts capture qualitatively different trajectories of institutional change, but have been developed independently of each other and thus lack coherence with regard to the institutional dimensions they consider. To overcome this, we use a new but already widely cited framework that allows for different directions of change, which is Thelen's (2014) framework of 'varieties of liberalization'.

Thelen argues (*ibid.*, pp. 11-12) that the concept of liberalization as such is insufficiently differentiated to account for the various types of institutional change in advanced political economies since the 1980s, even as the main trends of change included some element that can rightfully be called liberalization. To resolve this impasse, she proposes to conceptualize liberalization as a decline on any of two dimensions: coordination and coverage. 'Coordination' here takes its meaning from the Varieties of Capitalism (VoC) literature (Hall and Soskice, 2001). It refers to institutions that facilitate the strategic coordination of economic actors rather than market competition, a good example being centralized collective bargaining. Coverage refers to who is included in the arrangements of coordination. For example, it is possible that only the core workforce enjoys the benefits of collective bargaining and other protective institutions while others are individually exposed to employer preferences.

Based on these two dimensions, Thelen (2014, pp. 12-14) identifies three ideal-typical trajectories of institutional change (see Figure 1). Deregulation consists of a dismantling of coordination capacities and a simultaneous decrease in coverage of existing institutions. In dualization coordinating institutions are maintained, but only a shrinking core of actors is covered by them. Finally, embedded flexibilization involves the introduction of more flexibility in the realm of coordination whilst retaining a high degree of coverage of protective institutions. As mentioned, the advantage of Thelen's framework is that it encompasses in a unified scheme differing forms of institutional change. While she developed the framework for more long-term change in political-economic models, we will show that it can be applied also to shorter-term change in a specific policy field. Yet, we have to adapt her framework in two ways.

First, Thelen (2014) has devised a two-dimensional space but she has explored only a few types of 'movements' within it. While this is entirely justified within the scope of her book, she

does not consider institutional change that combines decline in one dimension with an improvement on another dimension and she does not consider different starting points of change. Southern European political economies are characterized by a state-led model of coordination, in which the coverage of collective bargaining was relatively high before the crisis (see below). Yet, coverage of high dismissal protection and of generous social benefits is narrow and the protection for those left outside is often poor (Ferrera, 2010). This in turn constitutes the potential for a recalibration of protective institutions. To account for this, we propose to incorporate in Thelen's framework a fourth type of institutional change, which we name 'embedding flexibilisation' as opposed to already embedded flexibilisation. This policy change consists of a flexibilisation of coordination while improving coverage, which starts from a low level (see Figure 1).

- Figure 1 -

Second, we have to spell out the operationalisation of the two dimensions of change more specifically for the policy field under analysis. We will examine five key areas of labour market policy: unemployment benefits, active labour market policies (ALMPs), regulation of standard employment (especially dismissal protection), regulation of non-standard employment, and legislation on collective bargaining. Note that in this paper we are interested in government reforms. Therefore, we focus on public policy and not, for instance, the whole field of collective bargaining as shaped by the practices of unions and employers. Moreover, ALMPs are scarcely developed in Southern Europe and will consequently not have a large weight in the analysis.

In the framework used here, a high degree of coordination consists of centralized collective bargaining, generous unemployment benefits, and high dismissal protection of standard workers. While it may not be obvious why the latter two can be called 'coordination', in the VoC literature they are typical for Coordinated Market Economies (CMEs) as they encourage investment in specific skills and long-term employment relations (Estevez-Abe et al., 2001). The implication of coverage in this framework is first of all obviously coverage of unemployment benefits and of collective bargaining. Moreover, stronger regulation of non-standard employment contributes to 'coverage' as it discourages the expansion of a secondary employment segment. It may seem surprising that higher EPL for standard employment is interpreted as higher coordination, whereas higher EPL for non-standard employment contributes to coverage. But these are in fact very different types of regulation. The first generates protection for core workers, whereas the second regulates the realm of peripheral workers: lower regulation of non-standard employment

allows for easier hiring of workers that do not enjoy the same benefits as core workers. This interpretation is in line with Thelen (2014).

In the realm of ALMPs we distinguish between enabling programmes (such as counselling and training) and demanding measures (based on conditionality and sanctions) (Eichhorst et al., 2008). The former should be seen as increasing coverage as they help to bring unemployed into employment without constraining their coverage by unemployment benefits. The latter can arguably be seen as decreasing coverage. Although they may push the jobless into work they do so by threatening to withdraw benefits, and the jobs attained are often of lower quality. However, as ALMPs are underdeveloped in Italy and Spain this distinction is not vital for our analysis.

#### **4. Why Italy and Spain?**

The choice of Italy and Spain is motivated by substantive and theoretical relevance. Substantively, Spain and Italy are cases of major public interest. At the cusp of the Euro crisis their financial stability was seen at risk. In contrast to smaller Greece, Portugal, and Ireland, the size of their economies and banking sectors would make a full bailout practically impossible. Hence, in the eyes of many commentators reforms in these two countries were crucial for the survival of EMU (e.g. Costa, 2012). As the problems of the Eurozone are still not resolved, an understanding of the political economies of Italy and Spain under austerity remains particularly relevant.

From a theoretical perspective, there are two reasons why Italy and Spain are good cases for studying reform dynamics under austerity. First, both were exposed to intense external and internal reform pressures, but neither of the two was formally bailed out and subjected to official reform conditions. Even if both governments can be said to have been subjected to ‘implicit conditionality’ (Sacchi, 2015), in contrast to Greece, Portugal, and Ireland they formally retained a degree of autonomy that makes it still meaningful to study their choices. This makes Spain and Italy ideal test cases for the kinds of labour market reforms adopted under extreme austerity. To be precise, Spain did in fact enter a financial assistance program from the European Financial Stability Facility in July 2012 for the recapitalization of its banks. However, this was agreed several months after the major Spanish labour market reform discussed below, and did not include specific conditions outside of the financial sector, except a commitment to country-specific reform recommendations in the context of the Stability and Growth Pact covered by our discussion below. In addition to not being subjected to (pertinent) explicit conditionality, Italy and Spain were arguably able to exercise greater leverage than smaller peripheral economies vis-



á-vis exogenous reform pressures from EU institutions due to the size of their economies and the threat that their exit would have posed to the survival of the Eurozone. Second, the two cases have very similar political-economic models and welfare states (see below) (Molina and Rhodes, 2007; Ferrera, 2010). Together with the similarity in pressures in the context of the Euro crisis, there are good reasons to expect analogous reform trends. As, however, we do not find similar reforms in both countries, our case selection enables us, in the logic of a Most Similar Systems Design (Przeworski and Teune, 1970) with different outcomes, to identify the reasons for the differences in reforms.

In terms of time, we consider the period from 2010 until summer 2015 (completion of manuscript). Under the pressure of high interest rates on government bonds, many European states started around 2010 to implement fiscal cuts and structural reforms (Armingeon and Baccaro, 2012; Schmidt, 2012). The Euro crisis has ebbed down somewhat since 2012 when the president of the European Central Bank (ECB) pledged his institution will do ‘whatever it takes to save the Euro’, thus substantially reducing pressures on bond markets. Yet, pressure by EU institutions to comply with the fiscal guidelines of tightened European economic governance continues. The focus of our comparison is on the major labour market reform that each of the two countries adopted under very similar conditions in 2012.

The analysis will draw on legislative texts, other primary sources, secondary literature, and a few background interviews with country experts.<sup>2</sup>

## **5. The institutional and economic context**

This section outlines the main features of the two cases in terms of labour market policy and crisis trajectory, to establish background and context of the reforms. Italy and Spain present many structural similarities. Both are classified as South-European welfare regimes with strong familialism and have been described as ‘Mixed’ or ‘State-led’ Market Economies, where the state has a crucial role in enforcing economic coordination given fragmented and conflictual industrial relations (Molina and Rhodes, 2007; Ferrera, 2010; Schmidt, 2012).<sup>3</sup>

Their labour market policies contain significant commonalities. The Spanish and Italian systems of employment and unemployment protection are both strongly segmented, leading to a high incidence of non-standard employment – extraordinarily high in Spain and rapidly growing in Italy. This results from labour market reforms that, attempting to reduce unemployment, have created contractual flexibility at the margins by deregulating the use of non-standard contracts whilst leaving EPL for standard (open-ended, full-time) workers mostly untouched (Boeri, 2011).

In Italy non-standard employment has been significantly liberalized by successive labour market reforms since the mid-1990s (Berton et al., 2012). In Spain, temporary contracts have spread earlier, following their deregulation in 1984. Since the 1990s governments have in fact attempted to decrease the wide EPL gap between open-ended and temporary contracts (Dubin and Hopkin, 2014; Bentolila et al., 2012). Yet, the impact of those reforms on reducing temporality in the Spanish labour market has been negligible and labour market dualism remains marked, as testified by a high share of temporary contracts and by widespread lay-offs of temporary workers during the crisis. Hence, the historical trajectories of the Italian and Spanish labour markets differed, but the segmented state in which they entered the crisis was similar. Labour market policy has been a contested topic at the centre of political debate for at least two decades in both countries.

A similar segmentation is present in the unemployment benefit systems of both countries, characterized by high fragmentation with considerable protection gaps for the long-term unemployed, non-standard employees, and new labour market entrants. To be sure, there are differences. Indeed, Spain has social assistance schemes, although these differ between regions and tend to be meagre. Yet, in Italy such schemes, which provide last-resort assistance also to the unemployed, are mostly lacking (Ferrera, 2005). Moreover, the coverage of unemployment benefit used to be somewhat better in Spain. However, as Figure 2 shows, coverage in Italy has improved, partly as a consequence of gradual reforms improving unemployment insurance (Picot, 2012, pp. 72-80) and partly due to the extraordinary measures adopted at the onset of the crisis by the Berlusconi government. During the crisis the rates of unemployed who received unemployment benefits have been almost identical in both countries. Berton et al. (2012) confirm the limited access by young and non-standard workers to Spanish unemployment benefits and conclude that ‘the Spanish unemployment compensation system seems calibrated on standard workers’ (ibid., p. 119).

- Figure 2 -

The Spanish system of industrial relations was, up to the recent reforms, characterized by an intermediate degree of centralization in which about 70% of employees were covered by agreements at the sectoral or regional level, despite low levels of union density (17.6% in 2010) (Visser, 2015), whilst only 10% were covered by company-level agreements (OECD, 2010). Similarly, Italy was characterized by a high degree of centralization in collective bargaining as the sectoral level was dominant, covering around 80% of employees (Visser, 2015). Levels of

union density are however higher than in Spain, at around 36% (Visser, 2015). Moreover, Italy and Spain are both characterised by a medium to high level of wage coordination, mainly achieved through inter-associational coordination by peak associations and sometimes facilitated by state intervention (Visser, 2015).

All in all therefore, Italy and Spain had a high degree of coordination in labour market policy before the austerity reforms, with centralized collective bargaining, high dismissal protection and generous unemployment benefits for standard workers. At the same time, both states stood relatively low on the coverage dimension for three of the four pertinent indicators: low coverage of unemployment compensation, deregulated employment protection of non-standard workers, and underdeveloped ‘enabling’ ALMPs. Coverage of collective bargaining by contrast was relatively high. Yet, as both states scored low on three out of four elements of this dimension, it is appropriate to regard them as starting from low coverage levels before the austerity reforms.

When the economic crisis hit Spain, unemployment leapt from 8.2% in 2007 to 24.5% in 2014, even though GDP contraction was not so large compared to other European states (Eurostat, 2015). The impact was especially strong on labour market outsiders, such as temporary workers whose contracts were not renewed. The importance of the construction sector and real estate bubble contributed to this negative employment performance (Bentolila et al, 2012). The unemployment increase led to rising public expenditure on unemployment benefits, due also to the decision in September 2009 by the Socialist government to introduce a new temporary unemployment assistance scheme for the long-term unemployed who had exhausted their ordinary benefits entitlement (EIRO, 2009).

Unemployment growth in Italy was less steep, from 6.1% in 2007 to 12.7% in 2014, in spite of a similar GDP decline (Eurostat, 2015). The crisis’ employment impact was cushioned by the use of short-time work (STW) schemes, which subsidize the pay of temporarily redundant workers in large industrial firms. Their duration was extended virtually indefinitely by the centre-right Berlusconi government, and discretionary extensions relaxed their realm of applicability. As in Spain, this led to a sharp increase in expenditure on passive LMPs (Sacchi et al., 2011), and higher job losses and insecurity were also concentrated among atypical workers. Despite some differences in employment performance, in both countries the crisis brought into sharp focus the disproportionate vulnerability of the peripheral workforce.

Both countries were also threatened from 2010 to 2012 by high interest on government bonds, driven by rising public deficits and international markets’ scepticism regarding governments’ capacity to service their public debt. Perez and Rhodes (2014, pp. 193-194)

account for some of the historical differences in fiscal policy between the two countries. Spain entered the crisis with a low and Italy with a high level of public debt. Spanish general government debt was 47% of GDP in 2008 and rose to 67% in 2010, the equivalent figures in Italy were 113% in 2008 and 125% in 2010 (OECD, 2015). During the crisis Spain ran higher public deficits than Italy. Average general government net borrowing between 2008 and 2013 was 8.6 % of GDP in Spain and 3.6% in Italy (OECD, 2015). Yet, given the high debt stock, financial markets and EU institutions were highly nervous about the Italian public budget as well so that the external austerity pressure both countries faced was similar.

## **6. Deregulation in Spain**

Despite the severity of Spain's unemployment increase in the crisis, the Socialist (PSOE) government, under José Zapatero, initially considered labour market reforms unnecessary (Molina and Godino, 2013). However, as unemployment and public deficit worsened, the European Union increasingly applied pressure on the Spanish government to adopt structural measures to address the worsening economic situation and the decline in financial markets' confidence in the performance of the Spanish economy. The Eurogroup meeting of May 2010 concluded demanding that the Spanish government implement strong austerity measures. This led to the approval of numerous budget cuts, followed in June 2010 by a labour market reform, the Real Decreto Ley 10/2010. The reform was unilaterally passed by the government after negotiations with unions failed, and was strongly criticized by unions, which staged a general strike in response (Hamann, 2013). The decree was ratified by parliament in September 2010 (Act 35/2010).

This reform aimed to halt employment decline and address labour market segmentation by modifying EPL to encourage the use of open-ended contracts over temporary ones. Acceptable reasons for economic-motivated dismissals of permanent employees were broadened and redundancy pay for dismissals with 'objective reasons' reduced. For dismissals judged by courts as unfair, the reform widened the conditions under which employers could choose to pay monetary compensation instead of reinstating the worker.

Required advance notices for economic dismissals were shortened and the use of special 'employment-promotion' open-ended contracts with lower severance pay, easier dismissal proceedings (so-called 'express dismissals') and lower compensation for unfair dismissals was facilitated. Meanwhile, regulation of temporary contracts was somewhat tightened by making their use marginally more restrictive and increasing severance pay in case of non-renewal. A

limit of three years for the duration of some temporary contracts was also imposed. Therefore, this first reform combined retrenchment in the coordination dimension (through lower EPL) with an improvement on the coverage dimension (through more regulation of non-standard employment).

Social dialogue between the government and unions was briefly restored after the June 2010 reforms. This led to the approval of RD Ley 3/2011 in February 2011, the only labour market intervention in this period based on an agreement between the government, the two main unions (UGT and CCOO) and the main employer federation (CEOE). In an attempt to strengthen activation and favour the labour market re-integration of unemployment benefit recipients, the law stipulated the requirement for unemployment benefit claimants to sign a ‘Personal Employment Agreement’, committing them to follow a personal itinerary of job search, counselling and training developed by the public employment services. These requirements, however, did not differ substantially from previous policy (EIRO, 2013). The reform was linked to the decision not to extend an unemployment assistance benefit that had been temporarily introduced in response to the crisis. It was replaced by a temporary active labour market program of requalification for those unemployed who had exhausted entitlement to ordinary benefits. It focused on compulsory participation in job search counselling and training activities, and complemented by an income transfer of €400 per month for a maximum duration of six months (slightly lower than the previous €420; Mato, 2011). From the analytical perspective of our framework the reform is ambiguous as it replaced one benefit with a stricter new benefit but put also somewhat more emphasis on counselling. Yes, the restrictive (workfare) side prevails, implying a modest negative shift on the coverage dimension.

Negotiations between the government and the social partners broke down again over the subsequent reform of collective bargaining, which had been requested of Spain by the European Council recommendations on Spain’s National Reform Programme of 2011 (European Council, 2011). The government thus intervened unilaterally once more in July 2011 with the RD Ley 7/2011. This reform represented the first intervention in the area of collective bargaining, as it established the precedence of firm-level collective agreements over industry-wide agreements, unless explicitly overruled by the latter. The measure notably reduced coordination in the Spanish system, where the primacy of sectoral collective agreements was deeply established in practice.

Despite opposition from the social partners, the reforms were considered by domestic commentators and European institutions alike not far-reaching enough and had no immediate impact on deteriorating unemployment (Bentolila et al., 2012; Dolado, 2012). As a consequence,

and in reaction to further pressures by the European institutions, the new conservative (PP) government, elected in November 2011 with Mariano Rajoy as prime minister, announced further labour market reforms. The employer federation (CEOE) and the main unions (CCOO and UGT) were offered the possibility of agreeing on the content of proposals, but when agreement failed, the government pressed ahead unilaterally with a major reform in February 2012, RD Ley 3/2012. The reform was opposed by PSOE and unions, but having a single-party majority in parliament the government had few problems in pushing it through.

The RD Ley 3/2012 intervened more radically than the previous reform in EPL, modifying legislation for both individual and collective dismissals. It abolished the ‘express dismissal’ procedures, expanded by the previous reform, and reduced compensation in case of unfair dismissal for *all* workers on permanent contracts. This intervention represents an unprecedented reduction in the level of dismissal protection for employees on permanent contracts. The clauses for justified economic dismissals were further simplified, the requirement for administrative approval of collective dismissals eliminated, and the timeframe for consultation on dismissals between employers and worker representatives reduced, thus considerably easing dismissal processes and reducing unions’ capacity to negotiate conditions for dismissed employees.

The 2012 reform also intervened on flexibility in entry. It repealed ‘employment-promotion’ contracts and created instead a new open-ended contract with a one-year trial period with unrestricted dismissal possibilities and no severance pay. This new contract is supposed to favour labour market entry of disadvantaged workers, but leaves them unprotected during their first year.

Moreover, the 2012 reform further decentralized collective bargaining by establishing the absolute priority of firm-level agreements over industry-wide agreements. It also allowed employers to unilaterally change contractual conditions at firm-level, including wages, for productivity or competitiveness reasons, which constitutes a considerable shift in control over working conditions towards employers (Dubin and Hopkin, 2013). The principle of ‘*ultraactividad*’, a cornerstone of the Spanish industrial relations system that sanctions the automatic extension of an expired collective agreement until the concerted approval of the new one, was also abolished. This has two implications. First, it forces social partners to speed up negotiations and may compel unions to accept worse contractual conditions (Clauwaert and Schömann, 2013). Second, the expiring of collective contracts without a renewal is likely to push down the number of employees covered by collective bargaining agreements. So far, bargaining coverage data is only available until 2013 (Visser, 2015), which does not evidence a decline yet –

although it is also too early to tell. Yet, data from the Spanish Ministry of Labour (2016) shows that among newly signed collective agreements the proportion of sectoral agreements has declined (from 89.4% in 2012 to 85.5% in 2014), while the number of firm-level agreements increased (from 9.1% to 11.8%). Therefore, we see the expected decentralization taking place.

The Rajoy labour market reform therefore constitutes a comprehensive retrenchment of institutions of coordination. The decentralization of collective bargaining, the deregulation of dismissal protection and the higher internal flexibility of employers all point in this direction. Somewhat ambiguous is the introduction of the new contract type with no dismissal protection in the first year, but arguably this only constitutes a new insecure contract type. In addition to declining coordination, the abolishing of the principle of *ultraactividad* might lead to a drop in coverage of collective bargaining.

Since 2012, no new major intervention into the labour market has been introduced. In fact, unemployment has slowly declined (from 26.1% in 2013 to 24.5% in 2014) and employment increased as economic growth recovered (Eurostat, 2015). Yet, the quality of newly created employment has been poor, with around 80% of new jobs created between the first quarter of 2013 and the first quarter of 2015 being temporary (INE, 2015). Long-term unemployment has also continued to rise, making up 62.1% of total unemployment in 2014 (ILO, 2014).

Overall, the thrust of the labour market reforms under austerity in Spain was a clear retrenchment of institutions that contribute to the strategic coordination of economic actors, especially by decentralizing collective bargaining and deregulating dismissal protection of workers in standard employment (see Table 1). On the second dimension, coverage, the implications are slightly more mixed. Under the centre-left government the modest reregulation of non-standard employment equates to a small improvement in coverage, while the slight expansion of ALMPs was counterbalanced by the non-renewal of a temporary unemployment assistance scheme. By contrast, the fact that the subsequent, conservative government abolished the principle of *ultraactividad* had a stronger impact as it led to diminishing coverage of collective bargaining. Therefore, the reforms not only led to a dismantling of coordination but also to declining coverage, which in Thelen's (2014) terms is the encompassing deregulation-type of liberalization.

## 7. Embedding flexibilisation in Italy

Following the initial crisis management, which relied on the expansion of pre-existing policies to deal with the negative employment impact (Sacchi et al, 2011), Italy's situation changed dramatically in 2011. The rise of interest on government bonds, combined with high public debt, low productivity, and meagre growth intensified pressures for structural interventions. In August 2011, as Italy's position on international markets worsened, a letter sent to the Italian government by ECB incumbent and elected presidents Trichet and Draghi (2011) demanded reforms of labour market policy along with other structural reforms and spending cuts. This was the beginning of a process of 'implicit conditionality' through which EU institutions applied pressure on the Italian government (Sacchi, 2015). Whilst seen at the time as an intrusion in Italy's domestic political authority, it has been argued that domestic policymakers used the ECB demands as an expedient to promote reforms in areas that had previously been object of vehement opposition, especially by unions (Sacchi, 2013a). Indeed, to address the ECB requests, the Berlusconi government approved within the same month an emergency austerity budget (Decree-Law 148/2011) that included in its Article 8 a reform of collective bargaining regulations, which allowed company agreements to diverge not only from sectoral agreements, but also from legislation on dismissals and employment law. This constituted a considerable decline in coordination and undermined the organizational power of unions by allowing plant-level representatives to sign agreements deviating from unions' directives. Still, the measure was less radical than the Rajoy reform in Spain because the general priority of national sectoral level agreements over local ones was retained, and no power granted to employers to unilaterally change work conditions without the agreement of local union representatives.

This reform focused solely on collective bargaining. In a letter to the European institution in October 2011 Berlusconi promised to adopt a more comprehensive labour market reform by May 2012 (Financial Times, 2011). However, as Italy's position on international markets worsened, the Berlusconi government resigned in November 2011 in an attempt to restore confidence in Italy's capacity to tackle its sovereign debt. This led to the appointment of a technocratic government headed by Mario Monti and supported by a parliamentary majority including the main centre-left and centre-right parties.

The Monti government proceeded to adopt in June 2012 a major labour market reform, the so-called 'Fornero Reform' (Law 92/2012), named after the labour minister Elsa Fornero. This reform followed a major reform of old-age pensions aimed at restricting pension expenditure. The labour market reform was hailed at the time as a flagship policy of the technical



government, supposed to deliver far-reaching changes where many reforms had failed throughout the 1990s and 2000s. The contents of the reform were initially negotiated with the main unions (CGIL, CISL and UIL) and the main employer federation (Confindustria), but the unions could not agree on a common position regarding the government proposal to lower dismissal regulations for workers on open-ended contracts. After months of back-and-forth, prime minister Monti eventually decided to proceed without union consent, declaring that ‘no one has the power to veto’ the reform (La Repubblica, 2012a). Yet, the unions retained influence on the final reform. At an early stage they made the government withdraw its plan to terminate the extraordinary STW scheme (La Repubblica, 2012b). Later the largest union (CGIL) maintained its opposition to the deregulation of dismissal protection for standard workers. With the support of the major centre-left party (PD), they managed to tone down the original government proposal (La Repubblica, 2012c). Finally parliament passed the reform under a vote of confidence in June 2012, with the votes of the government parties, although a high share of the main centre-right party (PDL) either abstained or voted against the reform.

The part of the reform most contested by the unions and the left fraction of the PD was to weaken the protection of workers on open-ended contracts in firms with more than 15 employees against unjustified dismissal. This protection is enshrined in Article 18 of the 1970 Workers’ Statute, and often identified as a key source of Italian labour market rigidity and a major achievement of the labour movement respectively. With this change the 2012 reform succeeded where a previous attempt in the early 2000s under Berlusconi had failed. Before the reform, if a judge ruled that a dismissal was unfair or unjustified, the worker was allowed to choose between monetary compensation and full reinstatement in their previous position, retaining seniority and receiving all monthly salaries and social security contributions for the period between dismissal and reinstatement. Particularly the latter point created uncertainties for employers about potential costs of dismissals, and constituted a source of institutional dualism as Article 18 does not apply to workers in small firms nor most atypical contracts. The reform reduced the possibility of reinstatement to cases of discriminatory dismissal and those for which the supposed economic or disciplinary reason is found to be ‘manifestly non-existent’. In addition, the payment of missed wages in case of reinstatement was capped at 12 months. For cases no longer covered by the possibility of reinstatement the maximum monetary compensation was raised. In our conceptual scheme, this change amounts to a retrenchment in coordination-facilitating institutions.

Regarding EPL for temporary contracts, Law 92/2012 explicitly aimed to reduce the incidence of precarious temporary work and eradicate instances of ‘bad flexibility’ (La Repubblica, 2012d). To this effect, the repeatability of fixed-term contracts was discouraged by

extending the ‘cooling-off’ period between two consecutive ones, and employer contributions to unemployment insurance for workers on fixed-term contracts increased. The reform also introduced new tests in order to combat ‘pseudo self-employment’. Furthermore, an attempt was made to limit abuse of apprenticeship contracts by employers, as these contracts enjoy a series of fiscal benefits. While the reform re-regulated and dis-incentivised temporary contracts, it nonetheless eliminated the necessity to provide a reason for establishing a first fixed-term contract of up to one year of duration.

Notable changes were furthermore introduced in the unemployment protection system. Ordinary unemployment insurance was replaced by a new instrument, the ASPI (Social Insurance for Employment). The benefit level of ASPI is marginally higher than the previous ordinary benefit, and the law envisages gradual increases of its maximum duration. Apprentices are fully enrolled in the new scheme; otherwise, eligibility requirements and coverage remained virtually unchanged. However, another new instrument, the ‘Mini-ASPI,’ was created to cater to workers with reduced contribution records. By replacing the previous ‘Reduced Requirements Benefit’, the Mini-ASPI eliminates the two-year minimum qualifying period requirement for benefit eligibility, thus significantly enlarging the pool of potential beneficiaries to recent labour market entrants. Sacchi (2013b) estimates that this reduced the number of uncovered workers in case of job loss by almost two thirds, helping in particular temporary agency workers and fixed-term workers. The benefit level is the same as ordinary ASPI, but the duration of Mini-ASPI is much shorter.

Finally, despite the government’s original intention to eliminate it, the extraordinary STW scheme was maintained for firms already covered, and new STW funds, co-managed by social partners and regional authorities, were made mandatory in all sectors for firms employing more than 15 workers. While, therefore, extending coverage to more sectors, institutional dualism between workers employed in large as opposed to small firms persists.

Regarding ALMPs, the Fornero reform intervened only marginally. It re-established the principle, already present in legislation, by which eligibility of unemployment benefits terminates in case a recipient refuses without good reason an adequate job offer or to participate in ALMP measures. The overall re-design of ALMP and Public Employment Services, historically underdeveloped in Italy, was delegated to later interventions, which did not take place as the Monti government came to a premature end after the centre-right withdrew its support in December 2012. In sum, the negative impact of this reform on coordination by deregulating dismissal protection of standard contracts is combined with notable measures to improve coverage: by re-regulating non-standard employment and by extending coverage of

unemployment benefits and STW benefits. While some elements of the reform had been demanded by policy experts for a long time (Berton et al., 2012), it was only now that external pressures and the political support in parliament provided the conditions for them to be adopted.

After the elections in February 2013 a new government was formed under prime minister Enrico Letta, with the parliamentary support of the PD and the PdL as well as smaller centrist parties. PdL (renamed *Forza Italia*) aborted its parliamentary support in November 2013, but a part of PdL split off and maintained its government support. In February 2014 Matteo Renzi succeeded Letta as prime minister through a coup within the PD. Renzi's government was under pressure due to continued high unemployment and low economic growth. Soon the government introduced a decree law (DL 34/2014), which deregulated the use of fixed-term contracts and apprenticeships and thus partly undid some of the re-regulation of non-standard employment the Fornero reform had introduced. In our framework this constituted a lowering of coverage. The decree appears to have been part of a political bargain that involved at the same time the introduction of a tax bonus for low-earners. Moreover, it was seen as a low-cost and quick way to keep unemployment in check (Picot and Tassinari, 2015).

A more substantial reform bill, the so-called Jobs Act, was passed later in 2014 with the votes of the government majority. This bill pursued a direction similar to the Fornero reform, by extending unemployment insurance and unemployment assistance, improving public employment services, and further reducing dismissal protection for workers in open-ended contracts. First, in unemployment insurance, the Jobs Act has merged the ASPI and Mini-ASPI of the Fornero reform and extended maximum durations. Moreover, it introduced on a pilot basis a new means-tested unemployment benefit for those not covered by unemployment insurance and limited the use of short-time work benefits, which are often used as a functional equivalent to unemployment benefits (Picot, 2012). Hence, part of the expansion of coverage by unemployment insurance and assistance were paid for by scaling back other entitlements (similarly in the case of the Fornero reform). Yet, this still constituted higher coverage as the strengthened schemes are the more widely accessible ones. Second, the Jobs Act aims to set up a National Employment Agency unifying and modernising currently regionally fragmented public employment services. Third, the politically most controversial part of the reform introduced a new open-ended contract with dismissal protection that increases over time, to be applied to all new hires on open-ended contracts. Over time it will substantially undercut the rules for dismissal protection under Article 18 of the Workers' Statute, especially by excluding the possibility of reinstatement after economic dismissals if they are ruled to have been unjustified. In addition, the reform and the accompanying budget law introduced fiscal incentives for new

hires on open-ended contracts and dis-incentivised dismissals through a lump-sum contribution to unemployment insurance. Other elements of the reform include provisions to introduce a national minimum wage, measures to improve work-family reconciliation, and more functional flexibility for employers (Picot and Tassinari, 2015).

Overall, the Jobs Act combines, just like the Fornero reform, a cut in coordination with an extension of coverage (see Table 2). More generally, the thrust of the labour market reforms in Italy has therefore been to deregulate dismissal protection of standard workers and to improve and modernize the system of unemployment protection. In our conceptual framework this corresponds to flexibilisation in terms of coordination and an ‘embedding’ in terms of coverage. Regarding the effects of extended unemployment benefit coverage, Figure 2 (above) shows that the decline in the beneficiary rate, most likely caused by an increasing share of long-term unemployed who exhausted their benefit entitlements, slowed down between 2012 and 2013. More revealing is that the number of unemployment insurance recipients, included in the beneficiary rate, rose more quickly (by 10.9%) between 2012 and 2013 than the number of redundant STW benefit recipients (by 1.8%; OECD, 2015).

- Table 2 -

## **8. Comparative discussion and conclusion**

Contrary to much of the literature that highlights labour market liberalization, plain and simple, under austerity, we find that two countries under similar circumstances have in fact followed different paths. In Spain, the reforms under the Socialist government until 2011 were still balanced by including a re-regulation of temporary employment. Yet, the major reform introduced under the conservative PP in 2012 was a comprehensive attack on labour market institutions, including radical de-centralization of collective bargaining, deregulation of employment protection, and higher internal flexibility for employers. All this weakens the capacity for strategic coordination in the Spanish labour market. Moreover, by abolishing automatic extensions of collective contracts the number of covered workers is set to shrink. Therefore, the Spanish case corresponds to what Thelen (2014) calls deregulation and to the general image of labour market reforms under austerity found in the literature and public debate.

The Italian case is different. Certainly, there are important similarities to the reforms in Spain. Italy has also decentralized collective bargaining (though not as much as in Spain) and has deregulated dismissal protection of standard workers. Yet, the distinctive feature is that both

major reforms in Italy, the Fornero reform and the Jobs Act, included an improvement of unemployment benefits in particular by widening the range of workers covered by these benefits. In addition, the Fornero reform re-regulated non-standard employment, and the Jobs Act provided a legal basis to improve public employment services. Therefore, the reform tendency in Italy under austerity combines decline on the dimension of coordination with an improvement on the dimension of coverage and can be called embedding flexibilisation. For the Fornero reform this improvement of coverage may to some extent have been traded off against restrictions in old-age pensions, but not in the case of the Jobs Act. Moreover, pension expenditure continued to rise in both countries, while spending on unemployment benefits increased in Italy but declined in Spain (Eurostat, 2016).

This article has not systematically focused on explaining the different paths in Spain and Italy. However, our case selection reduces the range of possible explanatory factors. Both states had similar political-economic models and similar labour market segmentation. Both states faced similar pressures from rising unemployment, low economic growth, and pressure from international financial markets as well as EU institutions regarding public debt and competitiveness. The comparison suggests that the involvement of the centre-left is crucial for reforms that counter-balance flexibilisation with an improvement of protection for labour market outsiders. Both major reforms in Italy were supported by the centre-left, first through their parliamentary support of the technocratic Monti government then by being the leading party of the government coalition under Renzi. In both cases the PD was the main parliamentary force to facilitate the reform, acting in coalition with the centre-right. When adopting the Fornero reform only a part of the main centre-right party, PdL, voted for the reform; for the Jobs Act it was a splinter party of the former PdL that supported the reform; therefore, the partisan composition was similar. By contrast, the major reform in Spain was introduced under a single-party conservative government. It is also notable that the more moderate previous reforms under the Spanish Socialists combined flexibilisation with improved protection similarly to Italy. The influence of the parliamentary centre-left in Italy was backed up by the fact that unions are still stronger in Italy than in Spain as has been shown to matter already in the previous crisis phase (Perez and Rhodes, 2015).

When applying the analytical perspective proposed by Amable and Palombarini (2014), the reforms in Italy can be seen as an attempt by the PD to consolidate a new social base consisting of skilled middle and upper classes. The decision to decrease EPL for insiders whilst increasing coverage for outsiders could thus help to attract consensus from sections of the middle-class that may support a redistributive and activating welfare state but not traditional ‘pro-worker’ policies

such as high EPL (cf. Häusermann et al, 2015). By contrast, the Rajoy reform in Spain is in line with what they describe as neoliberal rupture, which aims to draw support from the self-employed, small businessmen, and managers.

While the differences in the reform trajectories can be ascribed to domestic politics, the mentioned similarities, in particular deregulation of coordination, follow from the demands by EU institutions of ‘structural reforms’ and are pushed by financial market pressure on government bond interest rates (cf. e.g. Sacchi, 2015).

Our study has two main implications. The first is that even under intense austerity pressure different trajectories of labour market reform are possible, including better coverage for those marginalized from the labour market. The pressure from international markets and EU institutions certainly has favoured liberalization, broadly speaking. But this liberalization can take different shapes. In particular, it can combine a flexibilisation of strategic economic coordination with an extension of coverage. Second, domestic politics still matter. Although further research is necessary on the politics of labour market reforms under austerity, we find that the power of centre-left parties pulls labour market reforms toward embedding flexibilisation rather than full-out deregulation. This does not mean that right-wing parties will never introduce improvements of protection under austerity, but a sustained effort to balance flexibilisation with an extension of coverage is not to be expected by single-party conservative governments. On the dimension of coordination, changes in the basis of left-wing parties support coalitions away from the traditional working class (cf. Gingrich and Häusermann, 2015) may explain why they pursue policies of labour market flexibilisation similar to right-wing governments. However, fully explaining this similarity falls beyond the scope of our framework and requires further research.

Our article has also made a theoretical innovation by applying Thelen’s (2014) framework systematically to a comparison of labour market reforms and by adapting the framework to encompass more types of changes. In particular, we pointed out that a decrease on one of the two dimensions can be accompanied by an increase on the other dimension and that starting points can of course vary. This proved particularly relevant for the South-European context that starts from a low level of coverage, thus yielding scope for improvement on this dimension.

Finally, we would like to add two notes of caution from a normative point of view regarding the desirability of ‘embedding flexibilisation’ as found in Italy. First, while we focused on directions of change on two dimensions, extent and design of changes needs of course to be assessed. In particular, the Jobs Act included a far-reaching deregulation of dismissal protection,

partly designed to send a symbolic signal to investors and EU institutions by tackling a widely perceived 'rigidity' of the Italian labour market. It is questionable whether the extent to which the reform deprives workers of effective protection against unfair economic dismissal, on top of the more moderate and reasonable Fornero reform, is justified. Second, while fiscal austerity continues to depress economic demand potentially virtuous institutional reforms, such as embedding flexibilisation, are unlikely to alleviate the double problem of unemployment and precarious employment.

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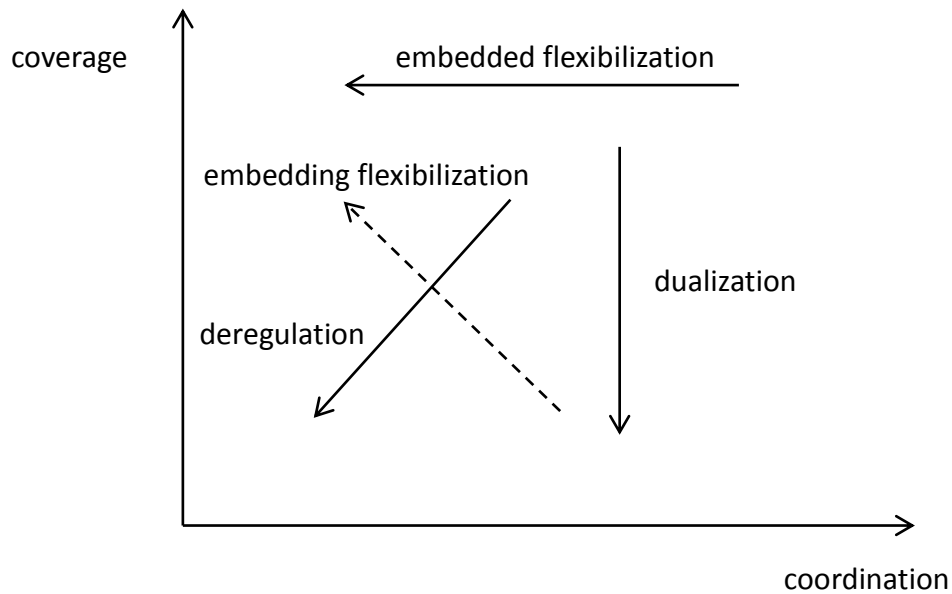
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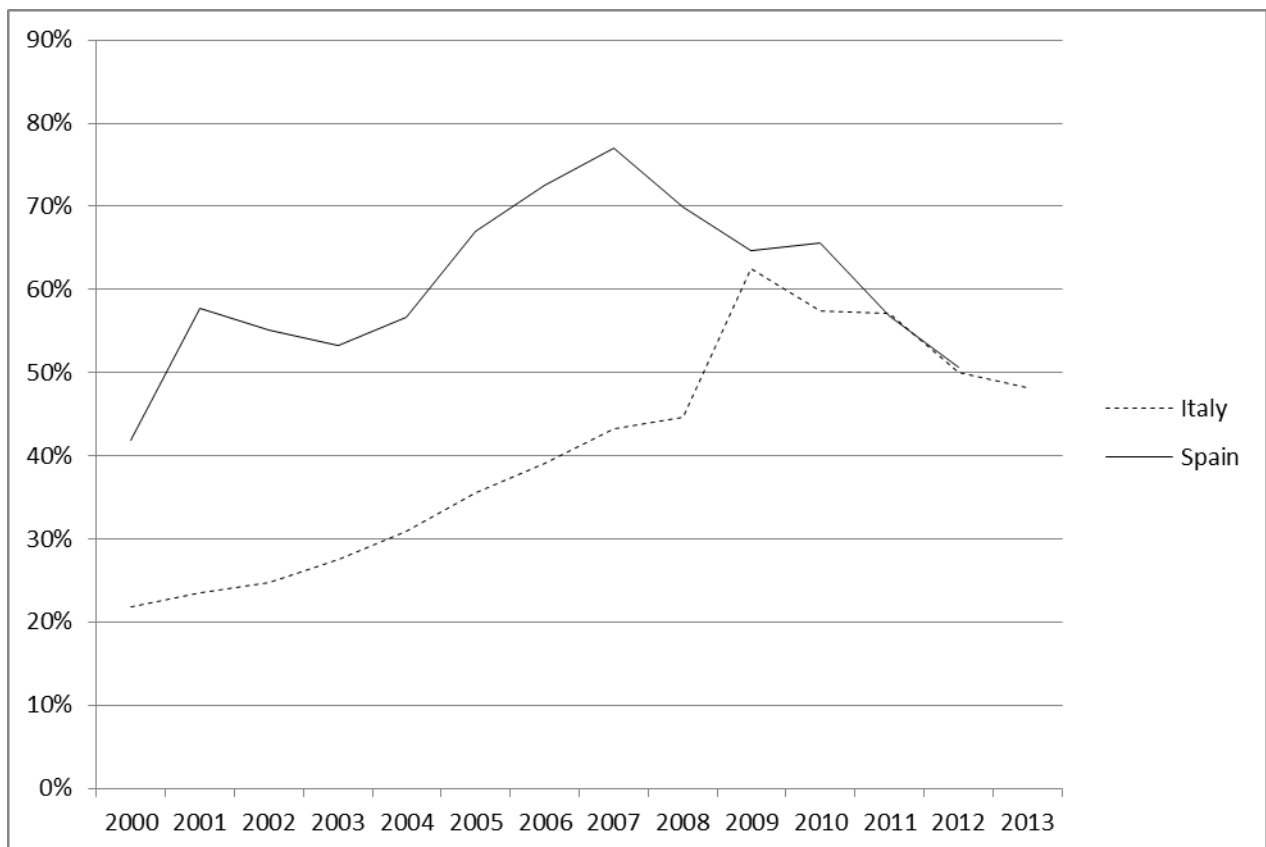
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**Figure 1** Ideal-typical trajectories of institutional change

*Source:* adapted from Thelen (2014, p. 13).

**Figure 2** Unemployment beneficiary rates, Italy and Spain, 2000-2013

*Source:* authors' calculations based on OECD (2015). The beneficiary rates are the number of recipients of out-of-work income maintenance as a percentage of the total number of unemployed.

**Table 1** Labour market reforms in Spain since 2010

Government	Reform	Content	Implication by dimension of liberalization	
			Coordination	Coverage
Socialist (PSOE)	RDL 10/2010	Deregulation dismissal protection	-	
		Reregulation of fixed-term employment		+
	RDL 3/2011	Modest workfare		(-)
		Non-renewal of unemployment assistance scheme		-
	RDL 7/2011	Decentralization collective bargaining	-	
Conservative (PP)	RDL 3/2012	Deregulation dismissal protection	-	
		New contract type without dismissal protection in first year		(-)
		Decentralization of collective bargaining	-	
		Abolishing of automatic extension of collective contract ( <i>ultraactividad</i> )	-	-
		Higher internal flexibility for employers	-	

**Table 2** Labour market reforms in Italy since 2010

Government	Reform	Content	Implication by dimension of liberalization	
			Coordination	Coverage
Centre-right	DL 148/2011	Decentralization collective bargaining	-	
	L 92/2012	Deregulation dismissal protection	-	
Technocratic (supported by major centre-right and centre-left parties)		Reregulation of non-standard employment		+
		Broader coverage of unemployment and short-time work benefits		+
		Modest commitment to ALMPs		(+)
	DL 34/2014	Deregulation temporary employment		-
Left-right coalition led by centre-left	L 183/2014	Longer durations and higher coverage of unemployment benefits		+
		Modernization public employment services		+
		Incentivization open-ended contracts		+
		Deregulation dismissal protection	-	



## Endnotes

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<sup>1</sup> Exceptions are Hall (2014) and van Kersbergen et al. (2014).

<sup>2</sup> Interviews were conducted with academics from the fields of social policy, industrial relations and economics (from the University of Oviedo, University of Bologna, University of Bari) and with the director of an independent Italian labor market research institute.

<sup>3</sup> The original VoC literature presented two ideal types: Coordinated Market Economies and Liberal Market Economies (Hall and Soskice, 2001). Much of the more recent VoC literature has a more differentiated and dynamic understanding of politico-economic models (e.g. Thelen, 2014, p. 4). In the same vein, this article is not interested in discussing typologies of economic models as such. Of interest to us are, however, the similarities between our cases pointed out by the cited literature.